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Imagery, Affect, and Financial Judgment

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Abstract

Traditional theories of finance posit that the pricing of securities in financial markets should be done according to the quality of their underlying technical fundamentals. However, research on financial markets has tended to indicate that factors other than technical fundamentals are often used by market participants to gauge the value of securities. This phenomenon may be quite prevalent in markets for initial public offerings (IPOs), where securities lack a financial history. The imagery and affect associated with securities can be a powerful basis upon which to judge their worth.

Advanced business students in a securities analysis course were asked to evaluate a number of industry groups represented on the New York Stock Exchange in terms of a set of judgmental variables. After providing imagery and affective evaluations for each industry group, the participants judged the likelihood that they would invest in companies associated with each industry. Imagery and affective ratings were highly correlated with one another and with the likelihood of investing. Judgments of performance correlated poorly to moderately with actual market performance as

measured by weighted average returns for the industry groups studied. The results suggest that imagery and affect are part of a coherent psychological framework for evaluating classes of securities, but that framework may have low validity for predicting performance.



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